

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



Transmitted via e-mail

August 21, 2020

Ms. Beverly Brown, Owner/Manager
Sonora Water Company (SWC)
PO Box 2196
Columbia, CA 95310

Dear Ms. Brown:

Final Report Transmittal Letter—Review of Sonora Water Company’s 2019 Annual Report for the period of January 1, 2019 through December 31, 2019

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) has completed its review of Sonora Water Company (SWC) regulatory basis financial statements of the 2019 Annual Report filed with the CPUC, which comprise the balance sheet as of December 31, 2019 and related statements of income, and retained earnings. The final review report is enclosed.

We issued a draft review report on July 17, 2020. We conducted an exit conference on June 22, 2020 and discussed our review results with SWC’s management and its accountant. SWC concurred with UAB’s findings and recommendations and agreed to correct its accounting records. On July 1, 2020, SWC submitted the revised financial statements to the UAB to correct the material misstatements described in Appendix A of the review report. However, SWC did not provide written comments to the draft report. We are issuing the report as final. We will post the final review report on our website at <https://www.cpuc.ca.gov/utilityaudits/>.

Please provide a Corrective Action Plan (CAP) addressing the findings and recommendations no later than October 5, 2020. The CAP should include specific steps and target dates to correct the findings identified. Please submit the CAP to the UAB at UtilityAudits@cpuc.ca.gov, with a copy to Bruce DeBerry, Program Manager of Water Division, at Bruce.DeBerry@cpuc.ca.gov.

We appreciate SWC’s assistance and cooperation during the engagement, and your willingness to implement corrective actions. If you have any questions regarding this report, please contact Raymond Yin, Program and Project Supervisor, at (415) 703-1818.

Sincerely,

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

Ms. Beverly Brown, Owner/Manager

Sonora Water Company (SWC)

August 21, 2020

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cc: Mr. Saul Gomez, Deputy Executive Director, Office of the Commission, CPUC
Mr. Lucian Filler, Deputy Executive Director, CPUC
Ms. Masha Vorobyova, Assistant Director, UAB
Mr. Bruce Berry, Program Manager, Water Division
Mr. Raymond Yin, Program and Project Supervisor, UAB
Ms. Khusbindar Kaur, Senior Management Auditor, UAB
Ms. Sharmin Wellington, Public Utilities Regulatory Analyst V, UAB
Mr. Sam Niepoth, Staff Services Management Auditor, UAB

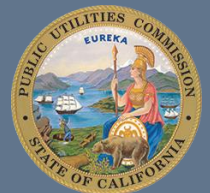


REVIEW OF FINANCIAL STATEMENTS

Sonora Water Company

For the Year Ended December 31, 2019

Utility Audits, Risk and Compliance Division
Utility Audits Branch
August 21, 2020



MEMBERS OF THE TEAM

Angie Williams, Director

Masha Vorobyova, Assistant Director

**Raymond Yin, CPA
Supervisor**

**Khusbindar Kaur, CPA
Lead**

**Sharmin Wellington, CPA
Staff**

**Sam Niepoth
Staff**

**A digital copy of this report can be found at:
<http://www.cpuc.ca.gov/utilityaudits/>**

**You can contact our office at:
California Public Utilities Commission
Utility Audits, Risk and Compliance Division
400 R Street, Suite 221
Sacramento, CA 95811**

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EXECUTIVE SUMMARY

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) conducted a review of the financial statements of Sonora Water Company (SWC) as of December 31, 2019, pursuant to Public Utilities (PU) Code, Sections 314.5, 314.6, 581, 582, and 584 that provides the CPUC the statutory authority to review or audit the books and records of the regulated utilities. We conducted this review in accordance with the standards prescribed under “Review of Financial Statements” in the Generally Accepted Government Auditing Standards (GAGAS).

Sonora Water Company (SWC) was incorporated in California on September 19, 1966. SWC is a Class D water utility with 112 active metered service connections. SWC serves customers in the vicinity of Tuolumne County, California. As a regulated water utility, SWC is required to prepare its financial statements on the accrual basis of accounting set forth in the Uniform System of Accounts (USOA) adopted in Decision (D.) 16-11-006 by the CPUC on November 16, 2016, which is a comprehensive basis of accounting other than the generally accepted accounting principles in the United States of America.

The purpose of this review is to obtain limited assurance as a basis for reporting whether we were aware of any material modifications that should be made to the financial statements in order for the statements to be in accordance with the USOA. In conjunction with our review of the financial statements, UAB also reviewed, for regulatory purposes, whether SWC complied with the following:

- a) PU Code Section 818 regarding obtaining CPUC approval before incurring any long-term debts.
- b) Timely filing of the 2019 Annual Report as required by the Water Division Memorandum dated January 7, 2020.

Based on our review, we are not aware of any material modifications that should be made to SWC’s revised financial statements in order for them to be in accordance with the accounting framework established in the USOA. For the review period, SWC timely filed its 2019 Annual Report in compliance with the CPUC directive from the Water Division but did not comply with PU Code Section 818 to obtain its long-term debt. UAB identified three material misstatements in SWC’s Annual Report originally filed with the CPUC’s Water Division, as described in the Appendix A – Review Findings and Recommendations. The three findings are summarized below:

- Finding 1: SWC improperly recorded court-ordered restitution of \$100,000 as an asset instead of a liability on its financial statements. In addition, SWC improperly reported connection fees in Account 470-Metered Water Revenue; recorded Advances for Construction of \$4,594 as Professional Services; and omitted Regulatory Commission Expense of \$2,910 from the Annual Report.
- Finding 2: SWC reported a long-term debt balance of \$45,655 on its initial Annual Report; however, SWC failed to obtain CPUC’s prior approval for the long-term debt as required by PU Code Section 818.
- Finding 3: SWC improperly utilized the cash basis of accounting for reporting its Metered Water Revenue, which was understated by \$29,987 in its Annual Report.

UAB discussed the above findings and recommendations with SWC at the exit conference. SWC concurred with the audit results and agreed to post UAB's proposed adjusting entries to correct the misstatements identified above. On July 1, 2020, SWC submitted the revised financial statements to the UAB to correct the material misstatements described in Appendix A of this report.

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

Ms. Beverly Brown, Owner/ Manager
Sonora Water Company (SWC)
PO Box 2196
Columbia, CA 95310

The Utility Audits Branch (UAB) of the California Public Utility Commission (CPUC) has reviewed the financial statements of Sonora Water Company (SWC), which comprise the balance sheet as of December 31, 2019, and the related income statement and statement of retained earnings for the year then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of SWC's management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, UAB does not express such an opinion.

Management's Responsibility for the Financial Statements

SWC's management is responsible for the preparation and fair presentation of its 2019 financial statements in accordance with the accounting framework established under CPUC's Uniform System of Accounts (USOA) for Water Utilities. SWC's management is also responsible for the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of its 2019 financial statements that are free from material misstatement, whether due to fraud or error. In addition, SWC's management is responsible for the development of its policies and procedures to ensure full compliance with applicable regulations and CPUC directives.

Accountant's Responsibility

UAB's responsibility is to conduct the review engagement in accordance with the standards applicable to reviews of financial statements promulgated by the Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with the accounting framework of the USOA. For regulatory purposes, UAB also reviewed whether SWC complied with PU Code Section 818 to obtain its long-term debts and whether SWC timely filed its 2019 Annual Report as required by CPUC's Water Division. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountant's Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with the accounting framework of the USOA. SWC's Annual Report originally filed with the CPUC's Water Division contained three material misstatements, which are described in Appendix A – Review Findings and Recommendations; these material misstatements have been corrected in the accompanying financial statements.

For the review period, SWC timely filed its 2019 Annual Report in compliance with the CPUC directive from the Water Division. However, SWC did not comply with PU Code Section 818 regarding obtaining CPUC approval before incurring any long-term debt.

Basis of Accounting

For regulatory purposes, the CPUC adopted, through Decision (D.) 16-11-006 on November 16, 2016, the updated USOA, which is a comprehensive basis of accounting other than the generally accepted accounting principles (GAAP) in the United States of America. The CPUC requires all water and sewer utilities to prepare their financial statements in accordance with the accounting framework of the USOA. SWC's financial statements were prepared based on this regulatory requirement.

We draw attention to Notes to the Financial Statements, in which we described the basis of accounting as well as the accounting differences between GAAP and the USOA. Our conclusion is not modified with respect to this matter.

Views of Responsible Official

On July 17, 2020, UAB provided a draft review report to SWC for comments. We conducted an exit conference on June 22, 2020 and discussed our review results with SWC's management and its accountant. SWC concurred with UAB's findings and recommendations and agreed to correct its accounting records. On July 1, 2020, SWC submitted the revised financial statements to the UAB to correct the material misstatements described in Appendix A of this report. However, SWC did not provide written comments to the draft report. We are issuing the report as final.

Other Matter - Submission of a Corrective Action Plan

SWC's management should submit a corrective action plan to the UAB at UtilityAudits@cpuc.ca.gov, with a copy to Bruce DeBerry, Program Manager of Water Division, at Bruce.DeBerry@cpuc.ca.gov no later than October 5, 2020. The corrective action plan should address how SWC will implement the recommendations and provide the timing of incorporating UAB's review adjustments to SWC's books and records. If SWC is unable to implement UAB's recommendations, the corrective action plan should state the reason(s) for not being able to implement any of the recommendations. SWC should use the amounts reviewed by the UAB as presented in this report as the basis to file its 2020 Annual Report with the CPUC.

Restricted Use of This Review Report

This review report is intended solely for the information and use by the CPUC and the management of SWC. It is not intended to be used and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

REVIEWED FINANCIAL STATEMENTS

Sonora Water Company **BALANCE SHEET (AS REVIEWED)** As of December 31, 2019

ASSETS	
UTILITY PLANT	
Water Plant in Service (Excluding SDWBA/SRF, Grant Funds)	\$223,466
Accumulated Depreciation of Water Plant	(64,074)
Net Utility Plant	<u>159,392</u>
INVESTMENTS	
Accumulated Depreciation of Non-Water Utility Property	(1,171)
Net Non-utility Plant	<u>(1,171)</u>
CURRENT AND ACCRUED ASSETS	
Cash	3,040
Accounts Receivable - Customers	29,987
Total Current and Accrued Assets	<u>33,027</u>
Total Assets	<u><u>\$191,248</u></u>
CAPITALIZATION AND LIABILITIES	
CORPORATE CAPITAL AND SURPLUS	
Common Stock (Corporations only)	\$43,300
Other Paid-In Capital (Corporations only)	93,000
Retained Earnings	(507)
Total Capitalization	<u>135,793</u>
LONG-TERM DEBT	
Long-Term Debt	41,441
CURRENT AND ACCRUED LIABILITIES	
Short-term Notes Payable	4,214
Other Current Liabilities	2,909
Advances for Construction	6,891
Total Current and Accrued Liabilities	<u>14,014</u>
Total Equity and Liabilities	<u><u>\$191,248</u></u>

(See independent accountant's review report and accompanying notes.)

Sonora Water Company
INCOME STATEMENT (AS REVIEWED)
For Year Ended December 31, 2019

OPERATING REVENUES

Fire Protection Revenue	\$1,292
Metered Water Revenue	255,530
Other Water Revenue	15,160
Total Operating Revenues	271,982

OPERATING EXPENSES

Plant Operation and Maintenance Expenses

Purchased Water	156,818
Transportation Expense	3,079
Other Plant Maintenance Expenses	20,194
Total Plant Operation and Maintenance Expenses	180,091

Administrative and General Expenses

Management Salaries	26,805
Office Supplies and Expenses	6,459
Professional Services	7,377
Insurance	1,300
Regulatory Commission Expense	2,910
General Expenses	4,043
Net Administrative and General Expenses	48,894

Total Operating Expenses 228,985

Depreciation Expense	6,025
Taxes Other Than Income Taxes	2,799
State Corporate Income Tax Expense	800
Total Operating Revenue Deductions	238,609

Total Utility Operating Income (Loss) 33,373

OTHER INCOME AND DEDUCTIONS

Non-Utility Income	756
Interest Expense (Excluding SDWBA)	(1,950)
Total Other Income and Deductions	(1,194)

Net Income (Loss) \$32,179

(See independent accountant's review report and accompanying notes.)

Sonora Water Company
STATEMENT OF RETAINED EARNINGS (AS COMPILED ¹)
 For Year Ended December 31, 2019

Retained Earnings, Beginning of Year	(\$49,663)
CREDITS:	
Net Income	32,179
SWC Prior Period Adjustment	16,977
Total Credits	49,156
DEBITS:	
Debits	0
Total Debits	(0)
Retained Earnings, End of Year	(\$507)

(See independent accountant's review report and accompanying notes.)

¹ UAB compiled the Statement of Retained Earnings based on the reviewed Balance Sheet and Income Statement, and other relevant financial data.

Sonora Water Company

NOTES TO THE FINANCIAL STATEMENTS

Regulated water utilities are required to prepare their financial statements on Accrual basis of accounting set forth in the Uniform System of Accounts (USOA) for Water Utilities adopted in Decision (D.) 16-11-006 by the CPUC on November 16, 2016, which is a comprehensive basis of accounting other than the generally accepted accounting principles (GAAP) in the United States of America. The following describes certain differences in accounting treatments between GAAP and USOA, the company's current accounting practices, and its compliance with applicable regulation and CPUC directives.

1. Purpose of Financial Information and Targeted Audience

The objective of preparing financial statements in accordance with GAAP is to provide information that is useful in making decisions about providing resources to the entity. Users of the financial information include existing and potential investors, lenders, and other creditors.

The purpose of using USOA to prepare financial statements is to have the utilities provide financial transparency of their water operations on a consistent basis. The primary user of the financial information is the CPUC for ratemaking and other compliance purposes.

2. Property, Plant, and Equipment

The USOA distinguishes the plant assets for water operations (i.e., Account 101, Water Plant in Service) from those for non-water operations (i.e., Account 121, Non-Water Utility Property and Other Assets), for ratemaking purposes.

(1) Depreciation Methodology

GAAP allows entities to elect a depreciation methodology of their choices, such as straight-line, double-declining balance, or sum-of-the-years digits depreciation method.

USOA requires utilities to use the "Straight-line remaining life method." "Remaining life" implies that estimates of future life and salvage value will be re-evaluated periodically and that depreciation rates will be adjusted to reflect any changes in estimates. Water utilities are required to comply with the CPUC's Standard Practice (SP) U-4-SM and SP U-4-M when determining depreciation accruals. Specifically, for the water plant with over \$100,000, the utility must maintain separate depreciation reserve by different plant accounts in accordance with Appendix B1 of SP U-4-SM; for the water plant under \$100,000, if the utility elects not to separate or maintain the depreciation reserve by accounts, it is appropriate to develop a composite value for remaining life for the entire plant in accordance with Appendix B2 or B3 of SP U-4-SM. The USOA suggested that all utilities maintain a separate accumulated depreciation subaccount for each depreciable plant account; and it is mandatory for water utilities having more than 500 customers.² The utility must obtain prior written approval from the CPUC for any practice deviates from the aforementioned SPs.

² D.16.11-006 dated November 10, 2016, General Accounting Instructions 4 on Page B14.

SWC used a straight-line depreciation methodology to depreciate its water plant. SWC reported Water Plant in Service of \$323,466 in its 2019 Annual Report, \$100,000 of which is attributed to court-ordered restitution. Therefore, the Water Plant in Service ending balance was adjusted from \$323,466 to \$223,466. SWC has revised its original 2019 annual report filed with the CPUC and posted the correcting journal entries to reflect the correct account balance in its revised financial statements.

(2) Asset Retirement

USOA requires that the water plant be recorded at the original cost. In USOA's depreciation schedule, the difference between the estimated cost of removal and the salvage value is included in the depreciable base to obtain the annual depreciation expense. When retiring an asset, the cost of removal will reduce the balance of Account 108, Accumulated Depreciation of Water Plant, while the cash received from the salvage value or sale price will increase the balance of Account 108, Accumulated Depreciation of Water Plant. The gain or loss from the asset retirement that is recognized under GAAP is accumulated in Account 108, Accumulated Depreciation of Water Plant under USOA.

SWC did not retire any asset during the review period. The utility plant is comprised of primarily water storage tanks.

3. Cash for Restricted Use

Under GAAP, if the restricted funds are considered to offset the current liability, the funds may be included as current asset classification. If the funds are set aside for use in the near future for the liquidation of long-term debts, payments to sinking funds, then the funds should be classified to non-current assets. If unsure of the timing of the use, the restricted cash can be classified as Other Assets.

Under USOA, the restricted funds are recorded to Account 132, Cash—Special Deposits, which should include cash amounts set aside from general corporate funds, deposited in a separate account with fiscal agents or others, and designated for a special use. A separate subaccount shall be maintained for each designated special use. Interest earned from this account shall be credited to Account 421, Non-Utility Income.

4. Advances for Construction

Under USOA, the advances for construction is similar to a loan for the construction work under GAAP. The construction contract must comply with the Main Extension Rule specified in the CPUC's SP U-17-W. Among other things, one of the requirements is "Advance Main Extension Contracts would run for 40 years, with refunds at 2 ½ percent per year."

Advances for Construction was received from Mountain Vista development and repayments are due upon the sale of each housing lot. Advances for Construction of \$4,600 were inadvertently reported as professional services expense, which resulted in a corrected balance of \$6,886. SWC has posted the correcting journal entries to its accounting records and reflected the correct account balance in its revised financial statements.

5. Contribution in Aid of Construction (CIAC)

CIAC account records non-refundable contributions of cash, land, or other property donated to the water utility to assist it in constructing, extending, or relocating its water system. The funds can be from governmental agencies and others. The balances in this account shall be written off over the period of its estimated service life by charging to Account 272, Accumulated Amortization of Contributions instead of a Depreciation Expense account, with contra credits to the appropriate subaccount of Account 108, Accumulated Depreciation of Water Plant.

(1) Facilities Fees

Facilities Fees are fees collected from ratepayers for the purpose of recovering a certain amount of revenue to offset certain facilities or improvements that are required to serve additional customers. Ordering Paragraph (OP) 3 of D.91-04-068 granted authority to Class C and D water utilities, and to districts of Class A and B water utilities with 2,000 or fewer service connections, to institute facilities fees as a part of their requests for a general increase in rates. Through Resolution W-4110, the CPUC granted authority to all Class D water utilities to file generic tariffs to charge fees for new connections for the purpose of generating funds to build a new plant or replace deteriorated plant. Facilities fees received by a water utility shall be deposited in Account 132, Cash–Special Deposits, and credited to Account 253, Other Credits. At the time these fees are used for water plant improvements, Account 101, Water Plant in Service shall be debited and Account 132, Cash–Special Deposits credited. Concurrently, Account 253, Other Credits shall be debited and Account 265.7, All Other Contributions in Aid of Construction credited. The annual depreciation and amortization of the facilities fees plant additions shall be debited to Account 272, Accumulated Amortization of Contributions, and credited to Account 108.3, Accumulated Depreciation of Water Plant–Other. The use of facilities fees should be in compliance with SP U-28-W.

6. Long-Term Debt

Water utilities are required to obtain prior authorization from the CPUC before incurring any long-term debt. PU Code Section 818, states that:

No public utility may issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months after the date thereof unless, in addition to the other requirements of law it shall first have secured from the commission an order authorizing the issue, stating the amount thereof and the purposes to which the issue or the proceeds thereof are to be applied, and that, in the opinion of the commission, the money, property, or labor to be procured or paid for by the issue is reasonably required for the purposes specified in the order, and that, except as otherwise permitted in the order in the case of bonds, notes, or other evidences of indebtedness, such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

SWC initially incurred a loan of \$117,000 on August 9, 2007, from Mother Lode Bank, which was later acquired by Oak Valley Community Bank in 2017 with an outstanding balance of \$67,157 at an interest rate of 5.75% maturing on July 9, 2027. The balance of Long-term Debt as of December 31, 2019 is \$41,441 and its current portion of \$4,214 is recorded in Short-term Notes Payables.

SWC used the water tank site as the collateral for the loan. SWC did not obtain CPUC's approval before obtaining the loan.

7. Water Utility Users Fee

PU Code, Sections 401 through 410 authorized the CPUC to set a fee annually to water utilities to cover the costs incurred by the CPUC in regulating them. USOA requires water utilities to credit regular operating revenue accounts with amounts of User Fees billed to customers and charge Account 688, Regulatory Commission Expense, with fees paid to the CPUC.³

SWC omitted CPUC Users Fee from its original 2019 Annual Report causing Account 688—Regulatory Commission Expense and Account 480—Other Water Revenues to be understated by \$2,910. However, SWC has posted the correcting journal entries to its accounting records and reflected the correct account balance in its revised financial statements.

8. Form of Financial Statements⁴

(1) Balance Sheet

Unlike the financial statements of other industries, the financial statements of regulated water utilities present the water plant as the first major caption on the asset side of the balance sheet, and capitalization is first on the liability side. Current assets and current liabilities are relegated to a comparatively unimportant position in the center of the balance sheet, rather than being placed prominently as in statements for non-regulated industries.

(2) Income Statement

The form of Income Statement reflects the classification of revenues and expenses in ratemaking. Operating revenues and expenses are referred to as “above the line” because they are allowable in ratemaking, and the result of deducting total operating expenses from total operating revenues is the operating income. Other Income and Deductions are referred to as “below the line” because they are applied after operating income and are not allowable in ratemaking. The “below the line” items include interest revenue, dividend income, other revenues that are from non-water utility operations and/or non-water utility properties, expenses that are unrelated to water utility operations, and interest expense (the interest expense is recovered through the authorized rate of return). The concept of “above the line” revenues and expenses being allowable in ratemaking affects the form of the income statement, the classification of revenues and expenses, and decisions of management in incurring expenses.

9. Exclusion of Statement of Cash Flows

Financial Accounting Standards Board specifies in its Statement of Financial Accounting Standards No. 95 that a Statement of Cash Flows is part of a complete set of financial statements under GAAP. However, Codification of Statements on Auditing Standards AU-C Section 800.A35 states, in part, that, “Special purpose financial statements may not include a statement of cash flows....” Since the USOA is an accounting framework other than GAAP for regulatory purposes, the

³ D.16.11-006 dated November 10, 2016, General Accounting Instructions 9 on Pages B18 and B19.

⁴ Regulated Utilities Manual—A Service for Regulated Utilities by Deloitte & Touché USA LLP, pages 36-37.

Statement of Cash Flows is not required by the CPUC and therefore excluded from this review report.

10. Compliance filing of 2019 Annual Report with the CPUC

PU Code, Sections 581, 582, and 584, and the CPUC's directive (i.e., Water Division's annual memorandum to water and sewer utilities) require all regulated water and sewer IOUs to file an Annual Report with the CPUC every year. For the year being reviewed, SWC has complied with these requirements.

APPENDIX

APPENDIX A— REVIEW FINDINGS AND RECOMMENDATIONS

Finding 1: Reporting Deficiencies

Condition:

UAB identified the following reporting errors:

- i. SWC recorded court-ordered restitution as an asset instead of a liability. SWC was ordered to pay restitution of \$100,000 to Tuolumne Utilities District. SWC initially recorded the restitution payments as Non-utility Property and Other Assets in Account 121 and later moved it to Water Utility Plant in Service in Account 101. The associated amortization of the court-ordered restitution was recorded as Accumulated Depreciation of Non-water Utility Property, Account 122, in the Annual Report. Restitutions are a liability of the utility; thus, should not be recorded as an asset.
- ii. SWC reported connection fees of \$12,250 in Account 470—Metered Water Revenue instead of in the proper account of Account 480—Other Water Revenue.
- iii. SWC inadvertently reported Advances for Construction as Professional Services Expense in Account 682, which caused both liabilities and expenses to be overstated by \$4,594.
- iv. SWC omitted CPUC Users Fee from the 2019 Annual Report causing Other Water Revenue in Account 480, and Regulatory Commission Expense in Account 688, to be understated by \$2,910.

Criteria:

The USOA in D.16-11-006 states that:

101. Water Plant in Service

A. This account shall include the original cost of all water plant owned and used by the utility in providing water service.

121. Non-Water Utility Property and Other Assets

A. This account shall include all property and other assets owned by the utility, but not used in providing water service, for which separate balance sheet accounts have not been provided.

122. Accumulated Depreciation of Non-Water Utility Property

This account shall reflect the depreciation and amortization accumulated on property not used in water utility operations.

A. This account shall be credited with amounts currently charged to accounts 426, Miscellaneous Non-utility Expense, representing currently accruing depreciation and amortization on property not used in water utility operations.

B. This account shall be charged with the amount of depreciation accumulated on items of non-utility property sold, abandoned, or otherwise retired.

480. Other Water Revenue

This account shall include revenue from water operations other than the delivery of water or provision of fire protection. This account shall be appropriately subdivided.

Fees for changing, temporarily shutting off or reconnecting services. Maintenance of appliances or repair of piping on customers' premises Rental income from water property.

Cause:

SWC was not versed in regulatory accounting guidelines and was unaware of the new USOA as prescribed in D.16-11-006, which caused material misstatements on several account balances reported in the Annual Report. Additionally, SWC did not have adequate review procedures in place to ensure accurate information is reported.

Effect:

Inaccurate reporting of Water Utility Plant in Service, Advances for Construction, Connection Fees, and Professional Services Expense, Regulatory Commission Expense balance distorted SWC's financial position as of December 31, 2019, which could impact the water tariff rates during the general rate case.

Recommendations:

SWC's management should familiarize itself with the USOA accounting requirements or seek professional help to establish and implement adequate internal control to comply with the CPUC directives and accurately report information in its annual reports by ensuring that:

- any liabilities against the Utility are properly classified in the Balance Sheet.
- connection fees are properly recorded in Account 480 – Other Water Revenues.
- payments for Advances for Construction are properly recorded as a reduction to the balance of Advances of Construction in Account 252.
- USOA guidelines are followed and CPUC Users Fee is reported as Other Water Revenues in Account 480 and related payments to CPUC are reported as Regulatory Commission Expense in Account 688.

Finding 2: Non-compliance with CPUC's Approval Requirements for Long-Term Debt

Condition:

SWC initially incurred a loan of \$117,000 on August 9, 2007, with Mother Lode Bank, which was acquired by Oak Valley Community Bank with an outstanding balance of \$67,157 at an interest rate of 5.75 percent maturing on July 9, 2027. SWC failed to obtain CPUC's approval before obtaining this loan, which caused SWC not complying with the requirements of PU Code, Section 818.

Criteria:

PU Code, Section 818 states that:

No public utility may issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months after the date thereof unless, in addition to the other requirements of law it shall first have secured from the commission an order authorizing the issue.

Cause:

Following a change of the Utility's ownership, SWC's current owner failed to prove SWC's prior owner had requested and obtained CPUC's approval before obtaining this loan as required by PU Code, Section 818.

Effect:

Non-compliance with CPUC's directives could expose SWC to undue liability.

Recommendations:

SWC should immediately file an advice letter with the Water Division of the CPUC to inform the Water Division about the long-term debt and follow Water Division's guidance accordingly. Going forward, SWC must comply with the requirements specified under PU Code, Section 818, by obtaining CPUC's prior approval before incurring any long-term debt.

Finding 3: Improperly Reporting Metered Water Revenue**Condition:**

SWC improperly utilized the cash basis of accounting for reporting its Metered Water Revenue on its Annual Report instead of the accrual basis of accounting as prescribed by the USOA. Metered Water Revenue was recorded when payments were received instead of when customers were billed. Thus, Account 470—Metered Water Revenue and Account 141—Accounts Receivable-Customers were understated by approximately \$29,987 per UAB's calculation.

Criteria:

General Instructions 2 of the USOA in D.16-11-006 states that:

A. The books of account of all water utilities shall be kept by the double-entry method, on an accrual basis. Each utility shall post its accounts monthly and shall close its books at the end of each calendar year.

Cause:

SWC was not versed in regulatory accounting guidelines as stipulated in the USOA, and thus did not comply with the USOA guidelines by using accrual basis of accounting.

Effect:

Inaccurate reporting of Metered Water Revenue distorted SWC's financial position as of December 31, 2019, which could potentially impact the water rates for SWC's ratepayers during SWC's rate-setting review process.

Recommendations:

SWC's management should familiarize itself with the USOA accounting requirements or seek professional help to handle its accounting and reporting matters. SWC should consistently apply the accrual basis of accounting when reporting its Metered Water Revenue in the Annual Report.